This Bill Analysis reflects the contents of the bill as it was presented in committee.

SENATE BILL 790:
Cape Hatteras/Gas Cities/Infrastructure Land

2013-2014 General Assembly

Committee:	House Finance	**Date:**	June 18, 2014
Introduced by:	Sen. Cook	**Prepared by:**	Cindy Avrette Committee Counsel
Analysis of:	PCS to Second Edition S790-CSRB-53		

SUMMARY: ***Senate Bill 790 would phase-in the sale tax on sales of electricity by the Cape Hatteras Electric Membership Corporation over two years. This change is time sensitive because the law it seeks to change becomes effective July 1, 2014. The House PCS to Senate Bill 790 makes technical changes to this provision at the request of the Department of Revenue.***

The House PCS to Senate Bill 790 also does the following:

- ***It would phase in the sales tax on sales of piped natural gas by the eight gas cities. The House passed this provision in its budget bill, Senate Bill 744, 7th edition, Section 37.4. This provision is time sensitive because the law it seeks to change becomes effective July 1, 2014.***
- ***It would modify the infrastructure property tax deferral program, enacted last year as S.L. 2013-130.***
- ***It would delay the change in the highway use tax base to include dealer administrative fees from July 1, 2014, to October 1, 2014. Both the House and Senate versions of the budget, Senate Bill 744, section 34.6, make this change. S.L. 2014-3 also made this change. This provision is time sensitive because the law it seeks to change becomes effective July 1, 2014.***

CURRENT LAW, BILL ANALYSIS, AND EFFECTIVE DATE:

Phase-In Sales Tax Rate

S.L. 2013-316 (*Tax Simplification and Reduction Act*) provided for the uniform taxation of all utilities. The Act repealed the franchise tax on electricity and increased the sales tax on electricity to the combined general rate of 7%. It also repealed the excise tax on piped natural gas and replaced it with a sales tax at the combined general rate of 7%. These sales tax changes become effective July 1, 2014.

Currently, Cape Hatteras Electric Membership Corporation (EMC) is not liable for franchise tax or sales tax on its sale of electricity. Other EMCs are subject to franchise tax and sales tax on their sale of electricity. Currently, the eight gas cities are not subject to the excise tax on their sale of piped natural gas. The eight gas cities are Bessemer City, Greenville, Kings Mountain, Lexington, Monroe, Rocky Mount, Shelby, and Wilson. Sales of piped natural gas by other providers are subject to the excise tax. S.L. 2013-316 did not retain these exemptions. Section 1 of the House PCS would phase-in the sales tax rate on these sales of electricity and piped natural gas over two years: effective July 1, 2014, the sales tax rate would be 3.5%; and effective July 1, 2015, the sales tax rate would be the same as the rate paid by other consumers of these products, 7%.

Cities receive a share of the sales tax imposed on piped natural gas. Under the former excise tax system, the amount was one-half of the amount of tax attributable to that city based on gas delivered to sales or

transportation customers in the city and gas received in each city by persons who have direct access to an interstate pipeline and who receive the gas for their own consumption. Beginning July 1, 2014, there is a different formula for distributing the proceeds to the cities. Moreover, the formula for gas cities differs from other cities. Subsections (b), (c), and (d) of this section clarify how the distribution is calculated for gas cities and provide that gas cities do not receive a distribution of the sales tax revenue derived from the reduced rate. A similar change is not necessary for the distribution of sales tax imposed on electricity for cities because there is no existing distribution impacted by the reduced rate for electricity sold by the Cape Hatteras EMC.

Electric membership corporations (EMCs) are not-for-profit entities that provide electric service in rural areas. North Carolina enacted legislation to allow EMCs in 1935 to promote electric service in the State. EMCs are not regulated by the Utilities Commission, but are governed by the board of directors that are elected by the customers of the EMC. Prior to 1965, each EMC was designated as a "public agency." As public agencies, the EMCs did not pay taxes on the sales of electricity by the EMCs. In 1965, the General Assembly enacted legislation clarifying the service area territories of EMCs and investor-owned public utilities. As part of the negotiation over the service areas, the legislation repealed the "public agency" designation for most of the EMCs. However, Cape Hatteras EMC retained its status as a "public agency" under the law. In 2000, the Department of Revenue informed Cape Hatteras EMC it would be required to remit sales tax on its sales of electricity.[1] Cape Hatteras paid the tax, but also filed suit for the return of taxes and clarification of its liability for the tax. In 2011, the North Carolina Court of Appeals held that Cape Hatteras EMC was not liable for the franchise or the sales tax on its sales of electricity.[2] S.L. 2013-316 specifically repealed the prior legislation that designated Cape Hatteras EMC as a "public agency" and stated "Cape Hatteras Electric Membership Corporation is subject to any other taxes to the same extent as other electric membership corporations established under Chapter 117 of the General Statutes.

Prior to 1999, the sale of piped natural gas was subject to sales and use tax, but sales by gas cities were exempt. In 1999, the sales and use tax on piped natural gas was replaced with a new excise tax. The new excise tax system preserved the tax exemption for gas received by a gas city for consumption by that city and for or gas delivered by a gas city to a sales or transportation customer of the gas city. A "gas city" is a city in this State that operated a piped natural gas distribution system as of July 1, 1998. There are only eight gas cities: Bessemer City, Greenville, Kings Mountain, Lexington, Monroe, Rocky Mount, Shelby, and Wilson. S.L. 2013-316 did not retain this exemption.

Modify the Property Tax Deferral Program for Site Infrastructure Land

S.L. 2013-130 created a property tax deferral program for sites with potential to be developed for office or industrial applications in order to encourage horizontal improvement so as to make the sites more readily adapted to those uses in a shorter timeframe. In order to qualify, the site must be zoned for office and/or industrial use, must consist of at least 100 acres, may not have a building permit for a primary building or structure issued for it, and must be currently enrolled in or have been enrolled within the previous six months in the PUV program.

Section 2 of the bill would remove the qualification that the property be enrolled in the PUV program. It makes a conforming change to the amount of taxes that are deferred. The amount of property tax liability that can be deferred is the portion of tax that represents the increase in the property value resulting from any existing horizontal improvement plus the difference between the property valued at its true value and the property valued as it would have been valued as if it were zoned the same as it was

[1] In 1965, only the franchise tax was imposed on the sale of electricity. In 1984, the General Assembly lowered the franchise tax on electricity and imposed a sales tax on sales of electricity.
[2] *Cape Hatteras Electric Membership Corporation v. Lay*, 210 N.C. App. 92 (2011).

in the calendar year prior to the time the application for property tax relief under this program was filed. The difference in value between property zoned as vacant or agricultural property and property zoned as industrial or office can be large. The change is effective for taxable years beginning on or after July 1, 2015.

The deferred taxes are carried forward in the records of the county and, if applicable, the city in which the property is located until the occurrence of a disqualifying event. A disqualifying event causes the current years' tax liability (without benefit of the program) and some previous years' deferred tax liability to be due and payable as follows:

- If, within five years of classification, an amount equal to the deferred taxes is not invested in improvements to make the land suitable for office and/or industrial use ("minimum investment"), the deferred taxes for the preceding five years are due and payable.
- If the minimum investment is made but the property is classified for 10 years in the program, the deferred taxes for the preceding five years are due and payable.
- If some or all of the land is rezoned for a use other than office and/or industrial use, all deferred taxes are due and payable.
- If land is transferred or a building permit issues for the land, the deferred taxes (for only that portion transferred or to which the permit applies) for the preceding year are due and payable. The remaining parcel continues to receive treatment under this classification, even if it no longer meets the size requirement.

Delay the Change in the Highway Use Tax Base to include Dealer Administrative Fees

In S.L. 2013-360, the Current Operations and Capital Improvements Appropriations Act of 2013, the highway use tax base was expanded to include any dealer administrative fees, effective January 1, 2014. Almost immediately, in S.L. 2013-363, the implementation of this change was delayed until July 1, 2014. Although the Current Operations and Capital Improvements Appropriations Act of 2014, Senate Bill 744, is in conference, both the Senate and the House passed Section 34.6 in that bill that would delay the implementation of this provision until October 1, 2014. S.L. 2014-3 rewrote the relevant highway use tax statute, effective October 1, 2014.

Section 3 of this bill makes a technical change by repealing the two provisions related to this change enacted last year, and thus allowing the change enacted in S.L. 2014-3 to become effective October 1, 2014. Without this change, the highway use tax base will change to include dealer administrative fees effective July 1, 2014, instead of the agreed upon date of October 1, 2014. If this provision is enacted, the corresponding budget section 34.6(a) of Senate Bill 744 will no longer be needed.